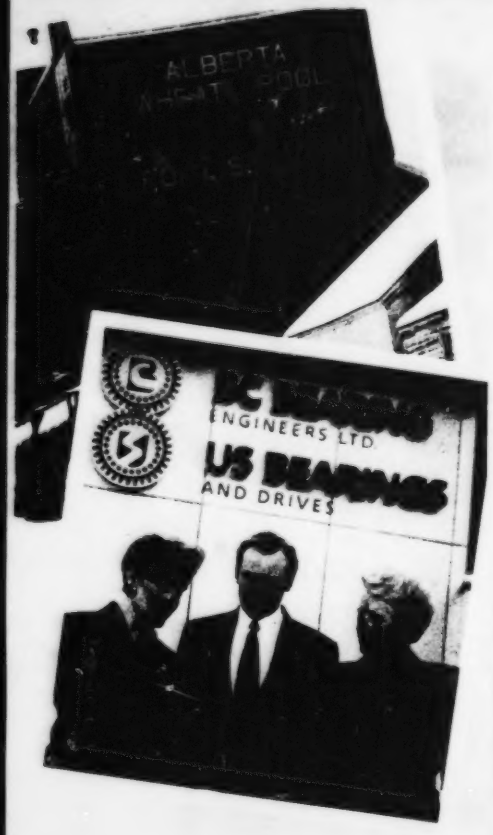
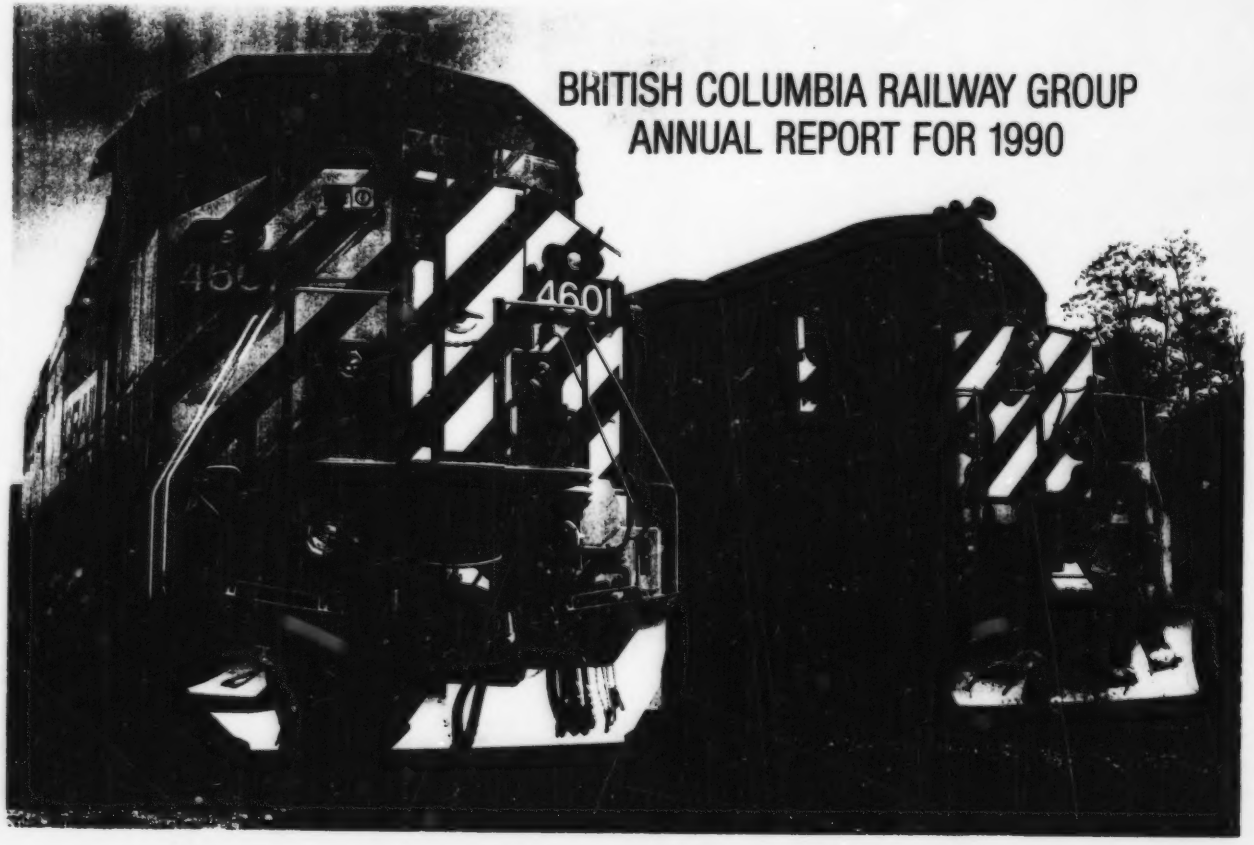
BRITISH COLUMBIA RAILWAY GROUP
ANNUAL REPORT FOR 1990





ON CUSTOMER FOCUS

In last year's annual report, I said that the BC Rail of the 1990s would evolve into a market-driven, customer-focused company and that our efforts would be concentrated on providing outstanding customer service at a competitive price on the one hand, while continuing to lower costs through ongoing productivity improvements on the other.

Soon after assuming executive responsibility for the company in 1989, it became evident, based on revenue and traffic trends alone, that if BC Rail was to continue to flourish as a successful business enterprise, a fundamental concern of both management and employees alike had to be the satisfaction of its present customers and through that, its ability to attract new ones.

After meeting most of our major shippers over the past year, reviewing the results of in-depth customer interviews and speaking with several hundred employees who have witnessed the railway lose ground to competing modes in today's deregulated environment, I remain convinced that the emphasis is in the right place.

In that respect, a great deal has happened during recent months. As many of our customers know, we completed a major customer survey in 1990, a large part of which dealt with perceptions of BC Rail and the levels of service and satisfaction we provide.

Let me say that the results were taken very seriously indeed and that over the past 12 months, employees at all levels have been working hard to create the kind of company our customers have told us they want—more responsive, more flexible and more sensitive to their needs for consistent, reliable and cost-effective transportation.

While there is more to accomplish, I will be reporting in the following pages the progress we have made towards that end and at the same time, seize the opportunity to reaffirm our company's absolute commitment to the principles of customer service and satisfaction first, foremost and always.

The customers of BC Rail, large and small—and whether they use our core freight, intermodal, telecommunications, passenger or any of the other services we provide—are the mainstay of our enterprise.

With that in mind, it gives me very great pleasure to dedicate our 1990 Annual Report to BC Rail customers everywhere who, when all is said and done, are our only reason for being here.

Paul J. McElligott
President and Chief Executive Officer

CORPORATE PROFILE

The British Columbia Railway group comprises three companies:

– British Columbia Railway Company, which holds investments in two subsidiary companies

– BCR Properties Ltd., which owns and manages the group's non-operating real estate assets and

– BC Rail Ltd., the group's operating railway company.

The Province of British Columbia is the sole shareholder of British Columbia Railway Company, which holds 100 per cent of the common shares of BCR Properties Ltd. BCR Properties Ltd. owns 75 per cent of the common shares of BC Rail Ltd., the remaining 25 per cent of which are held by British Columbia Railway Company.

The group is principally engaged in the transportation of forest products, coal, ore concentrates and other natural resources. It is also involved in real estate development, telecommunications marketing, road transportation and transportation consulting.

BC Rail operates 1,387 miles of trackage within British Columbia. It has interline connections to all rail-served points in North America.

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BOARD OF DIRECTORS

Gerry Strongman, *Chairman*
Victor Bowman
Winton Derby
E. Beverly Ellis
Jim Inkster
Edward John
Paul J. McElligott
E.A. Moffat
James T. Rabbitt, M.L.A.*

*Resigned December 19, 1990
Anthony Brummet, M.L.A. was appointed January 24, 1991

OFFICERS

Paul J. McElligott, *President and Chief Executive Officer*
Wayne C. Banks, *Vice-President – Marketing and Sales*
J.R. Clarke, *Vice-President – Finance and Information Services*
Brian Foley, *Vice-President – Human Resources, Engineering and Communications*
J.C. Trainor, *Vice-President – Operations and Mechanical*
Frank Trotter, *Vice-President – Strategic Planning and Business Development*
R.W. Young, *Vice-President – Real Estate and Administration and Corporate Secretary*

NOTICE OF SPECIAL MEETING

For Non-voting Preferred Shareholders

The Board of Directors and Management of BC Rail Ltd. cordially invite preferred shareholders to an informational meeting on June 11, 1991. The meeting will start at 9:00 a.m. and be held in the Resolution Room of the Lonsdale Quay Hotel, 123 Carrie Cates Court, North Vancouver, B.C.

The meeting is not a legal requirement and is offered as a courtesy to the company's preferred shareholders. Its purpose is to report on company activities and performance during 1990 and on the outlook for the current operational year. The informational meeting is open to the general public. It precedes the company's annual general meeting, which is open only to common shareholders, directors and officers of the company.

For further information, please call:
Ms. C.A. Lee (604) 984-5291

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FINANCIAL HIGHLIGHTS

	(Dollars in Thousands) 1990	1989
Operating revenues	$295,053	$328,953
Operating expenses	$237,289	$241,715
Operating income	$ 57,764	$ 87,238
Extraordinary item	–	$ (80,646)
Net income (loss)	$ 33,782	$ (16,057)
Total freight tonnage hauled	15,851,000	16,955,000
Employees at year-end	2,480	2,700

COVER
Early in 1990, BC Rail took delivery of 22 new General Electric C40-8, 4000 hp locomotives, which replaced 29 older Montreal Locomotive Works 3000 hp units built in 1970. New GE unit No. 4601, left, and retiring MLW No. 706 were photographed at the 'Dash 8' inauguration ceremony in Squamish. The remainder of the photographs, both on the cover and throughout this publication, are representative of BC Rail's many valued customers, whose participation and cooperation in the design and illustration of our annual report are gratefully acknowledged.

CHAIRMAN'S REPORT

There is no question that 1990 was one of the more difficult operating years the British Columbia Railway group has experienced for more than a decade. While revenues and operating income fell short of an acceptable return on investment, it is to management's credit that a net profit was accomplished at all.

For a variety of reasons which will be discussed elsewhere in the report, railway revenues declined by nearly 11 per cent over those of 1989. Despite every effort by management to reduce costs during the year, net income fell by nearly $31 million compared with 1989, before provision was made that year for an $80.6 million extraordinary charge.

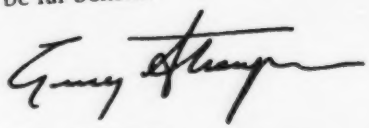
This clearly is a setback to the railway's aspirations and progress over the past few years. Nevertheless, it will be evident from the President's report and the accompanying narrative that many of the reasons for last year's results were quite unpredictable and beyond management's ability to control. I am confident, however, that the setback is temporary and that the railway's future continues to be bright.

During the year, a great deal of progress was made in creating a more efficient, responsive and service-oriented organization and I am optimistic that major benefits to the railway and its customers will be realized as the provincial economy regains momentum.

An inevitable side-effect of poor market conditions in any organization is the need to adjust the size of the workforce. No business enterprise can hope to sustain employment at constant levels when revenues and profitability are declining and as Mr. McElligott reports elsewhere, the company was obliged to reduce the number of positions during the year. While such decisions are always difficult to make, I know that the staff reductions were handled in a humane and generous manner.

In December, Hon. J.T. (Jim) Rabbitt, MLA, announced his resignation from the Board of Directors, following his appointment as Minister of Labour and Consumer Services earlier that month. Mr. Rabbitt was succeeded on the Board by Hon. A. J. (Tony) Brummet, MLA, whose appointment was announced on January 24, 1991. I would like to take this opportunity to thank Mr. Rabbitt for his valuable contribution and counsel to BC Rail. We look forward to working with Mr. Brummet and on behalf of my fellow members, I am delighted to welcome him aboard.

In the year ahead, the Board of Directors and executive management will be addressing means of returning the railway to a desirable level of profitability and sharpening the company's competitive edge. I am confident that the economy of the province will begin accelerating within a relatively short period of time and that the economic recovery of the railway will not be far behind.



Gerry Strongman
Chairman

PRESIDENT'S REPORT

Nineteen-ninety was a difficult year. Poor forest products markets, combined with abnormal railway operating conditions during the second half led to a substantial reduction in revenues and operating income.

Net income for 1990 was $33.8 million, compared with a 1989 net loss of $16.1 million. The previous year's net loss, however, resulted from an extraordinary charge of $80.6 million – for the write-off of the most northerly portion of the Dease Lake extension – against income of $64.6 million.

The reduction in revenues, from $319.9 million in 1989 to $285.5 million in 1990, underscores how closely the railway's fortunes are linked to those of its customers. The year was characterized by a steady decline in U.S. and Canadian housing starts, which by mid-year had translated into a severe downturn in the company's eastern rail lumber shipments, while throughout the year, a world oversupply of pulp kept shipments severely depressed. This situation was aggravated by an unusually strong Canadian dollar against its U.S. counterpart and poor industry profitability. As a result, pulp and woodchip traffic on BC Rail was significantly down from that of earlier years.

On a brighter note, however, work on the first phase of the railway's Takla extension, in northwestern British Columbia, was completed by year-end and revenue trains began operating in late December.

Further south, the company concluded a long-term real estate and transportation agreement with Cariboo Fibreboard Company, whose new plant in Williams Lake, B.C. is expected to be under construction by the spring of 1991. In Prince George, a new facility built by FMC Canada Ltd. began shipments of hydrogen peroxide by BC Rail.

In northeastern B.C., Louisiana-Pacific Corporation is in the final stages of

constructing a new pulp mill at Perry, which is scheduled to begin production during the second quarter of 1991. Efforts to recapture traffic lost in recent years to road transportation met with some success in 1990 and that, together with a strengthened core freight marketing capability will ensure such improvements continue. Early in 1991, the company's Intermodal Services business unit began taking delivery of new trailer-on-flat-car (TOFC) equipment. At the same time, more competitive intermodal rates and service packages were developed to attract freight traffic currently travelling by competing carriers.

There were encouraging signs too, outside the railway's core operations. Under the direction of our new Vice-President of Strategic Planning and Business Development, Frank Trotter, the company's Commercial Telecommunications business unit filed an application in July, 1990 to expand long distance voice and data transmission services in B.C., Ontario and Quebec, in a joint marketing venture with Lightel Inc. and Call-Net Telecommunications Inc., of Toronto. If the application is approved by the Canadian Radio-television and Telecommunications Commission (CRTC), the new venture will increase utilization of BC Rail's surplus microwave communications capacity, add significantly to telecommunications revenues and broaden the company's revenue base. The final outcome of the CRTC hearings, scheduled to begin in April 1991, will not be known until 1992 at the earliest.

Mr. Trotter joined the company in July. He brings a wealth of transportation and communications experience to BC Rail and I am delighted to welcome him as a member of the executive management team.

As part of an executive reorganization of the company in February, it also gave me a great deal of pleasure to appoint Walter Young to the position of Vice-President – Real Estate and Administration. To that point, Mr. Young had been General Manager of Real Estate and Corporate Secretary. In addition to his vice-presidential responsibilities, he will continue as Corporate Secretary.

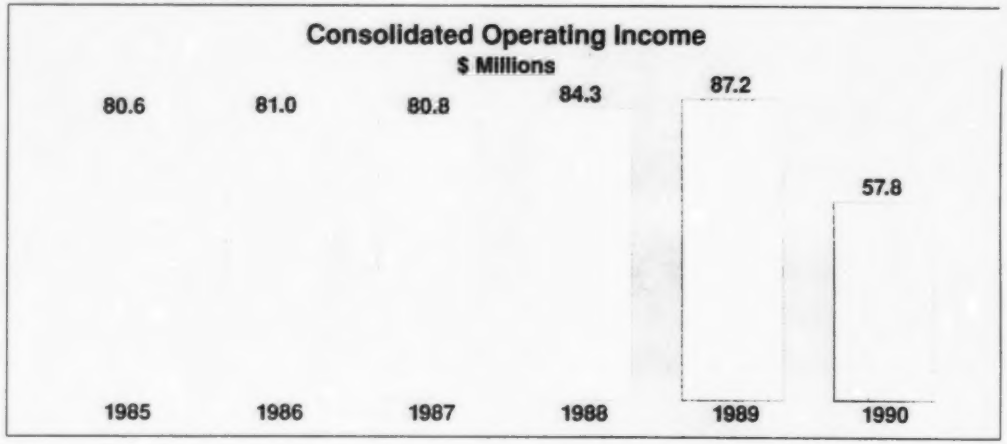
Mr. Young served previously in a number of senior marketing and administrative roles since joining the company more than 20 years ago.

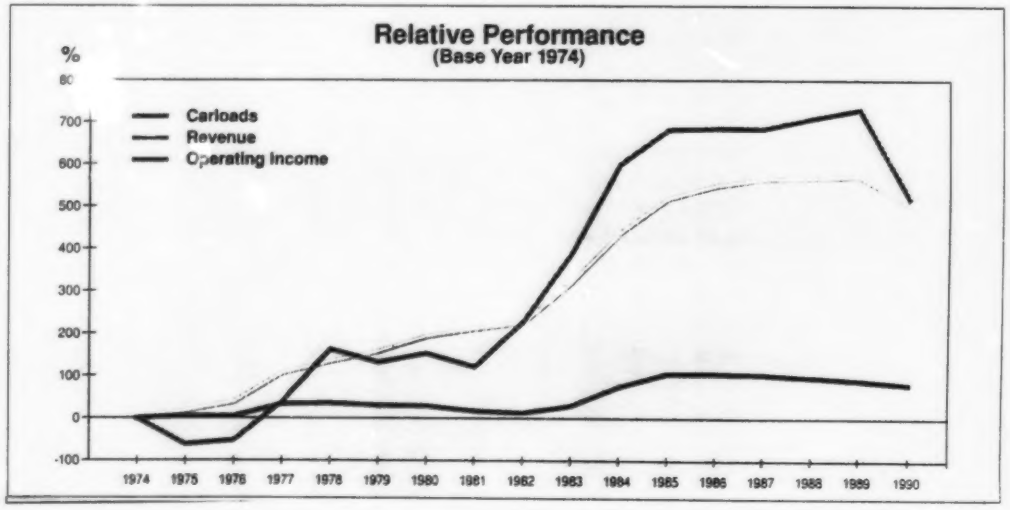
During July and August, both freight and passenger services were seriously disrupted by a series of native Indian rail blockades in which the railway was an innocent third party. The last of the blockades was followed almost immediately by the first employee strike action in more than 10 years, which lasted 25 days and led to a complete shutdown of railway operations during the month of September.

These occurrences, together with a prolonged series of floods, mudslides, rockslides and some of the worst winter conditions in recent memory, led to line closures that totalled 66 days during the course of the year. These events, combined with substantial one-time reorganization costs, had a severe effect on 1990 operating performance and contributed in no small way to the year's poor results.

During the latter part of the year, executive management initiated a strategic planning process involving employees from all divisions and departments of the railway. Ten interdepartmental task forces were formed near year-end. Their purpose was to analyze the company's present situation, its competitive strengths and weaknesses and the opportunities and challenges in the years ahead. Task force findings were presented to the executive group early in 1991. The planning process continues until a strategic direction for the company is finalized in mid-1991.

As a result of corporate re-structuring begun early in 1990, the company's activities and accounting systems have been segmented into six distinct business units in addition to the company's core rail freight business, each of which is accountable for its own performance. The six units identified are Car Management, which is currently being formed and will be responsible for fleet management and optimizing car hire revenues; Intermodal Services, the company's road-rail freight section; BC Rail Telecommunications, which commercially markets long distance voice and data communications services; International Rail Consultants, a joint venture with Sandwell Inc. offering railway consulting services outside B.C.; Real Estate, which is responsible for the management and development of the company's property assets and finally, Passenger Services which has now assumed full marketing and sales responsibility for the province's historic Royal Hudson steam train. This had previously been handled by an independent tour operator. The railway is also developing plans to market its fleet of lounge and sleeping cars for private charters under the name Summit Service. The renewed passenger marketing effort, which includes the railway's scheduled Cariboo train, will be supported by an international advertising agency appointed near year-end

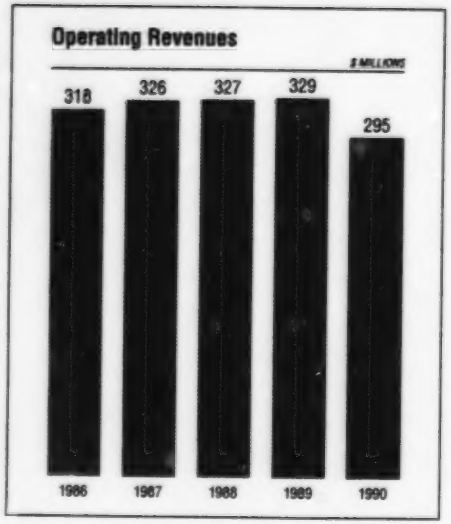


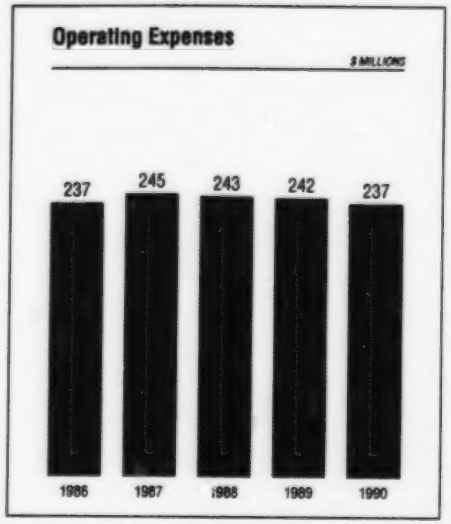


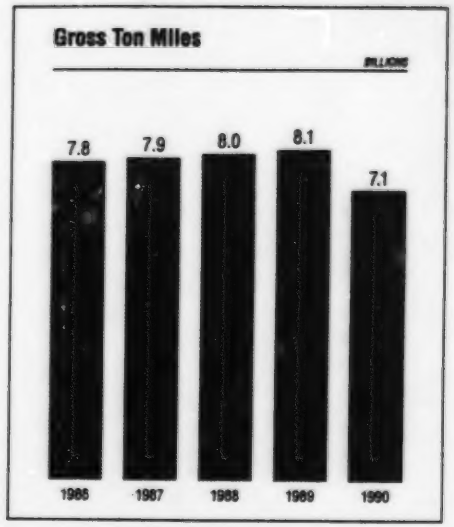
to develop a fresh new advertising and merchandising program. The unit's objective is to increase ridership and revenues while reducing subsidy requirements.

During the year and continuing through the early part of 1991, it became necessary to reduce the numbers of both union and management positions as a result of technological change, centralization of certain work functions and the decline in traffic and operating revenues. To the extent possible, staff reductions were accomplished by attrition and early retirement.

In view of the fact that the recession has now firmly taken hold in Canada and the United States, the immediate outlook for the commodities on which BC Rail depends for its revenues is not encouraging. Prospects for improvement in the first half of 1991 are slight. Nevertheless, the railway remains in sound financial and operating condition and is becoming appropriately sized for the competitive tasks and





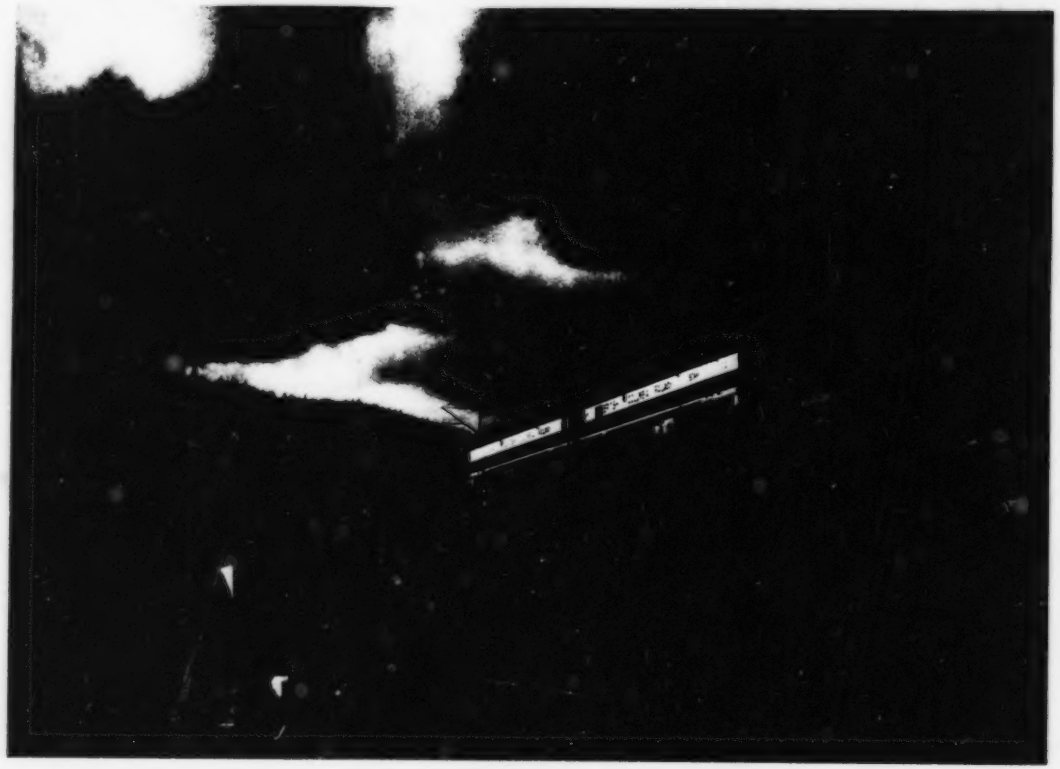


challenges that lie ahead.

In conclusion, I must say that I am most encouraged by our employees' response to the many challenges faced during the year, not the least of which were the changes necessary to move the company to its new operating philosophy. It was a difficult transitional year for all of us. I am grateful to employees for their efforts and continuing support. Many changes have taken place and I am confident we will meet the challenges that lie ahead to improve the railway's service and competitive edge.

Above all, I value most highly the loyalty and goodwill our customers have demonstrated through the year. Their understanding and support is vital during these transitional times but in the long run, it is they who will benefit most from the resulting, more efficient and more service-oriented BC Rail.

Paul J. McElligott
President and Chief Executive Officer



Electrified unit coal train in northeastern B.C.

THE YEAR IN REVIEW

A year during which the railway's operations were halted for the equivalent of more than two full calendar months can only be described as eventful—and it is doubly unfortunate that the 66 days of closures came during a year of poor commodity market conditions.

For all that—and despite the disappointing operating results—the news is by no means all bad. Many positive events occurred during the year—some of which brought immediate benefits to the railway and its customers while others can be regarded as investments in the future.

The year began with the completion of a strategic marketing study of core rail freight, the purpose of which was to determine the company's competitive position by means of extensive customer audits and other research.

Prior to the study's findings, the company had already begun strengthening its marketing and sales division. The division was reorganized to respond more quickly and effectively to customers' needs. Market-based pricing policies were developed during the year and within the various commodity transportation groups, staff were given more autonomy and empowered to react more quickly to customer needs.

In the months ahead, the company will be conducting follow-up customer audits to verify that concerns identified by the study, as well as during the normal course of business, are being addressed.

In northwestern British Columbia, reconstruction of the railway's Takla extension began in the spring and by year-end, the first phase of the project was complete. In consideration of traffic commitments by a consortium of forest companies, the company is investing $25 million in rehabilitating the line and in December, the first revenue-producing train operated from Lovell Cove, B.C., to Fort St. James. The investment will be recovered through freight rates over a 20-year contract period. When the second and final phase of the rehabilitation is complete in late 1992, the consortium will generate up to 13,000 carloads of logs annually. The completed line will extend 210 miles northwest of Fort St. James. The first phase, finished in 1990, covered the first 125 miles.

New traffic developing

Elsewhere, work is expected to begin soon on construction of a new fibreboard manufacturing facility in Williams Lake. During 1990, the railway's real estate and marketing units concluded a long-term land, track and transportation agreement with the Cariboo Fibreboard Company. Initial traffic when the plant becomes operational will amount to 1,250 rail carloads annually and increase progressively after that. The 500-acre development, on land leased from BC Rail, also includes a "co-generating" electricity plant, which will replace beehive burners and contribute to cleaner local air quality.

In Perry, B.C. – 10 rail miles east of Chetwynd—construction of a new pulp mill by the Louisiana-Pacific Corporation is nearing completion and expected to commence production in the second quarter of 1991. Rail access to the new facility is in place and when fully-operational, the new mill is expected to contribute approximately 2,000 carloads of freight each year.

In keeping with the company's continuing efforts to provide a safe, clean and environmentally-sound transportation system, executive management has approved a five-year environmental management plan prepared by the company's environmental engineering group. The group also played a major role during the year in the construction of an industrial waste storage facility in the railway's Squamish shops area, as well as a waste treatment system in the North Vancouver yard.

Hon. Rita M. Johnston, Premier and former Minister of Transportation and Highways, launching new Dash 8.

Deliveries of 22 new General Electric 4,000 hp diesel locomotives began early in 1990 and were completed by late spring. The new fuel-efficient units replace 29 older Alco engines, disposal of which progressed throughout the year, and form the basis of the railway's fleet renewal and modernization program. The program also includes fitting new Caterpillar engines to twenty-seven 1,800 hp yard locomotives, work on which is continuing in the Squamish shops. The inauguration ceremony for the new, General Electric 'Dash-8' locomotives was performed by Hon. Rita M. Johnston, MLA, who was the Minister of Transportation and Highways in 1990.

Passenger service showed encouraging growth during the first seven months of the year but overall ridership for the year was down as a result of the extended closures in the latter part of the year. Nevertheless, the passenger marketing effort is

intensifying and this year includes, for the first time, full responsibility for the Royal Hudson steam train service. In 1991, the company will unveil its new Summit Service, which will make available the railway's historic fleet of business cars for private charters and functions. During the year, the Cariboo passenger fleet—the self-propelled Budd cars that provide daily service between North Vancouver and the north central interior—was augmented by three additional units acquired from VIA Rail Canada. Near year-end, the company appointed J. Walter Thompson Ltd. as the advertising agency for BC Rail.

Track works continue

Aside from the Takla line rehabilitation program, engineering work was largely focused on the south end of the system and during the year, installation of an additional 41 miles of continuous welded rail—together with a major steel tie installation and wooden tie replacement program—was carried out on the Squamish subdivision. Rock stabilization, bank widening and bridge work were extensive systemwide, though the bulk of activity was concentrated on the Squamish subdivision between North Vancouver and Lillooet. The engineering department also continued with the upgrading of the Fort Nelson Extension, part of a long-term program to bring the line up to appropriate operating standards.

Modernization and expansion of the railway's North Vancouver yard facility included a major intermodal service and reload centre, which was completed on schedule in mid-year. The new intermodal facility, officially opened in June with ceremonies involving both employees and customers, greatly enhances the railway's road-rail capability.

The Mobile Yard Repair program successfully introduced in Prince George in 1988 is now also in place in the North Vancouver yard. The mobile units carry out minor repairs to freight cars as they arrive on site and reduce out-of-service time and shop congestion.

The railway's Mechanical department is actively seeking opportunities to contract work in and during the year, an agreement to upgrade 200 boxcars on behalf of the Procor Corporation was obtained. The contract is valued at approximately $1.5 million. Ninety-four of the cars were completed in 1990. The remainder will be completed in the coming year. In the department's locomotive shops, work also began on rebuilding a 1,000 hp yard locomotive for Alcan's Kitimat facility.

Non-contract work included the in-house upgrading of 100 bulkhead flat cars, which will convert the units into centrebeam flat cars. Centrebeam cars facilitate loading and improve customer efficiency. The conversions are being carried out in response to customers' stated preferences and work on an additional 150 cars will continue through 1991.

During the second half of the year, the company filed an application to the Canadian Radio-television and Telecommunications Commission (CRTC) to join with Toronto-based Lightel Inc. and Call-Net Telecommunications Inc. in providing long distance voice and data services between B.C., Ontario and Quebec. BC Rail has been engaged in marketing its surplus telecommunications capabilities for several decades. Hitherto, activities have been confined to private line services to business customers in B.C. Approval of the joint venture application will expand the company's tele-communications services and offers the potential to increase revenues. The railway's commercial telecommunications group is also investigating the possibility of expanding its intra-provincial network.

The company's non-commercial communications arm, which provides voice and data services for railway operations, continued through the year with its program of trackside radio coverage enhancement, the addition of six new train safety inspection systems and the upgrading of several level crossings. Work also continued on installation of the company's new digital communications system, which is expected to be operational as far north as Prince George by early 1992.

Turbulent economic times

While the company progressed on many fronts, setbacks began early in the year with poor market conditions for many of the railway's customers, which inevitably created a fall-off in freight revenues that continued throughout 1990. Market conditions were showing few signs of recovery at the beginning of 1991 and railway revenues for the year so far continue to be below normal levels.

Management remains concerned about the ultimate outcome of the Quintette Coal Limited reorganization. Northeast coal shipments account for approximately 20 per cent of the railway's revenues and we remain hopeful that a successful reorganization plan can be completed in 1991. The company's large investment in the project was predicated upon specific freight rates, transportation surcharges and traffic commitments over a 15-year term. Both tonnages and rates are lower than those originally anticipated and any deviation from existing levels will have a direct effect on future profitability.

In July and August, operations were severely disrupted by a series of native Indian blockades over issues which did not directly concern the railway. The end of the blockades was followed by strike action by the company's 1,700 unionized employees, which again brought the railway to a standstill for a further period of 25 days.

The matter was subsequently resolved by the involvement of an industrial inquiry commissioner and a union membership vote

on his recommendations. The validity of the recommendations and the unions' vote has been challenged in court by some of the unions and a final resolution is yet to come. Also still unresolved are some of the railway's proposals for improved productivity, one of which involves cabooseless operations and is critical to remaining competitive. It is expected that these will be decided by third party arbitration in 1991.

The labour dispute was followed near year-end by appalling weather conditions ranging from heavy rains and severe flooding, to heavy snowfalls and prolonged sub-Arctic temperatures. The heavy rains of November brought flooding, washouts and mudslides and in December, heavy snow and temperatures sometimes below -40°C seriously hampered operations.

The abnormal conditions created problems with locomotive traction motors and radiators and led to related failures of motive power and rolling stock, as well as frozen track switches and other outdoor equipment necessary to keep trains operating.

In the railway's main repair facility in Squamish, a severe windstorm caused substantial damage to the motive power shop which resulted in the shop roof being blown off. Because of the abnormally heavy snowfalls, maintenance and snowplough crews worked around the clock in some of the worst winter conditions in memory to keep trains running. Snow removal equipment and section crew costs in December hit record levels.

New directions

The company is well into the latter stages of a strategic planning process, designed to create a corporate plan for the railway and formalize its direction for the 1990s. As well as executive management, departmental managers are taking part as task force members whose preliminary findings were presented to the executive planning group early in 1991. The process is expected to be complete by mid-1991.

Information systems and applied technology continue to play an important role in the company's ability to satisfy customers' transportation requirements, BC Rail's operating efficiency and safety standards. Recent advances in data capture, communications technology and computerization offer opportunities for productivity gains and in 1990, a number of improvements were made to systems supporting the marketing and sales, operations and mechanical functions.

Several major customers established electronic document interchange systems; train movements and control were improved through the introduction of a computer-assisted dispatch system and throughout the year, work continued on the development of a train crew scheduling and monitoring system. On the shop floor, the company's Mechanical department finished testing a computerized work information collection system, which is scheduled for installation in 1991.

On May 1, the company departed from its traditional practice of awarding across-the-board management salary increases and instead, linked individual pay increases to job performance. Line management is now responsible for allocating salary budgets in a manner which appropriately rewards the achievement of company objectives by individual employees.

During the year, the company also initiated a 15-month project to revise the method by which management jobs are assigned to specific salary ranges. The new, computerized system will meet pay equity guidelines and replace the former method which has been in use for more than 20 years.

As a result of recommendations for pension plan improvements made by the pension committee in 1990, the company commissioned a study of the plan's competitiveness against comparable plans in the public and private sectors. Early in 1991, the Board of Directors approved certain amendments to the pension plan.

Dash 8 heading a southbound forest products train.

In addition to the railway's core rail freight business, BC Rail Ltd. comprises five operating business units, each of which is intrinsically related to the core business but tracked separately in terms of performance. A sixth, Car Management, is currently in the process of being formed and when it becomes fully operational as a separate unit later this year, it will have the responsibility for the enhancement and development of off-line car hire revenues and car fleet acquisitions and disposals. The following pages contain a brief description of the five business units already operational—Passenger Services, Commercial Telecommunications, Real Estate, Intermodal Services and International Rail Consultants. Together they represent less than 10 per cent of the companies' consolidated revenues, but each has encouraging growth prospects.

PASSENGER SERVICES

BC Rail's founding predecessor, the Pacific Great Eastern Railway, operated the company's first passenger train on January 1, 1914. The service was largely operated with conventional, locomotive-hauled equipment until the mid-1950s, when the railway took delivery of six self-propelled rail diesel cars (RDCs) from the Budd Corporation of Philadelphia. The fleet of RDCs—the mainstay of BC Rail's scheduled 'Cariboo' service—now comprises 12 units, nine of which have been completely rebuilt over the past five years. The remaining three have been recently acquired from VIA Rail and are currently being upgraded to BC Rail standards.

Passenger Services is one of seven separate business units within BC Rail. Like most passenger railways around the world it is not self-sustaining and currently receives operating and capital assistance from the government of British Columbia. As a result of renewed marketing emphasis and investment, however, ridership and revenues have been steadily improving over the past few years and the unit's stated objective is to increase revenues and ridership while minimizing the need for government operating subsidies.

As well as scheduled RDC service between North Vancouver and Prince George, Passenger Services is responsible for the operation and marketing of the historic Royal Hudson steam train excursion, which runs between North Vancouver and Squamish during the summer months. The magnificent Hudson class locomotive, designated 'Royal' after a sister unit hauled the royal train of King George VI and Queen Elizabeth across Canada in 1939, is a world-rated tourism attraction and a familiar summer sight along British Columbia's scenic Howe Sound.

Tour operator, centre, with Passenger staff.

Royal Hudson plans for 1991 include new family fares, pre-boarding, on-board and destination activities and entertainment. The steam train is also becoming increasingly popular for private and corporate charters—notably in the field of incentive travel.

In 1991, the railway's fleet of vintage business cars, hitherto reserved for line inspections, sales efforts and the recognition of long-service and retiring employees, are also being made available for private charter under the brand name Summit Service. The cars are elegantly furnished with lounge and sleeping accommodation, and staffed to offer first class dining for small to medium-sized groups in a unique, historical atmosphere. While Summit Service was not officially launched until the spring of 1991, early interest has been encouraging and a number of reservations have been booked.

Marketing of the three passenger services brands—Cariboo, Royal Hudson and Summit—will be strengthened by the recent appointment of a major international advertising agency, J. Walter Thompson Ltd. The agency was appointed early in 1991 and is currently working with the railway's

Summit class charter service, due in 1991.

passenger marketing and advertising departments in developing creative and media strategy.

Passenger Services works closely with on-line communities and since the early 1980s, a great deal of progress has been made in the development of destination accommodations and activities. The passenger unit is also playing an active role in the railway's strategic planning process and has identified a number of opportunities for new product development. Approximately 60 per cent of total Cariboo passengers comprise inclusive tour groups and tourists, who originate in eastern Canada, the United States and overseas.

During peak holiday seasons, passenger load factors are extremely high but as in other passenger transportation modes, they fall during the off-season. Seat sales and other marketing initiatives, however, do much to encourage off-peak travel and for those seeking an inexpensive alternative to road or air travel, the railway offers reliable, year-round transportation between Greater Vancouver and the north central interior.

COMMERCIAL TELECOMMUNICATIONS

BC Rail's Commercial Telecommunications business unit is responsible for marketing the railway's surplus microwave telecommunications capacity to outside users.

Among North American railways, BC Rail pioneered the use of microwave radio telecommunications and as early as the 1950s, train control and other internal communications needs were met by what was then the most advanced radio technology in service. While channel capacity was surplus to the operating railway's requirements, regulatory constraints prevented the company from actively marketing the surplus. With the exception of some leases to governmental organizations, serious commercial efforts to do so did not begin until 1985.

The new Commercial Telecommunications unit was formed at that time, with a mandate to broaden the railway's telecommunications revenue base in competition with established carriers. Since that time, the list of users has grown to include recreational and hospitality businesses in and around Whistler, B.C.; provincial and federal government departments and oil, gas, mining and forestry related companies in central and northeastern B.C.

BC Rail is currently engaged in upgrading its analogue system to digital microwave, the new industry standard. The new system is scheduled to be in operation as far north as Prince George by the first quarter of 1992. Commercial Telecommunications' contribution to group revenues rose during 1990, but at a slower rate than that experienced in earlier years. The unit offers competitive rates and innovative solutions to commercial users' telecommunications requirements although at the present time, its activities are restricted to the railway's operating area.

BC Rail offers telecommunications alternatives.

In mid-1990, however, BC Rail filed a joint application with Lightel Inc., a Toronto-based telecommunications company, to the Canadian Radio-television and Telecommunications Commission. If the joint venture is approved, the two companies, tentatively named BCRL, will be allowed to interconnect their networks in B.C., Ontario and Quebec to the Public Switched Telephone Network (PSTN) and the Unitel system, to provide public switched and dedicated voice and data telephone service.

The BCRL joint venture is designed to meet the growing demand for the diversity and information analysis that comes with switched long distance telephone service. BCRL also plans to provide a variety of value-added and specialized telephone services in the three provinces named. This will be provided over owned and leased facilities. In addition to BC Rail's continuing digital upgrade of its microwave system, Lightel has embarked on construction of a fibre optic communications network in B.C., Ontario and Quebec.

The combined corporate and technical strength of BC Rail Telecommunications and Lightel/Call-Net make BCRL well-qualified to understand Canadian business and residential telecommunications requirements, with particular strength in information processing for small to medium-sized businesses. Until recently, interconnection of private networks to PSTN for long distance services was restricted to members of Telecom Canada, as monopoly suppliers.

While approval and implementation of the BCRL application will add to BC Rail telecommunications revenues, the proposed BCRL services will represent only a small proportion of the total Canadian long-distance voice and data market.

Public demand for more extensive telecommunications competition has been growing dramatically in Canada over the past few years, spurred by developing competition and the growth of digital microwave and fibre optic networks.

REAL ESTATE DEVELOPMENT

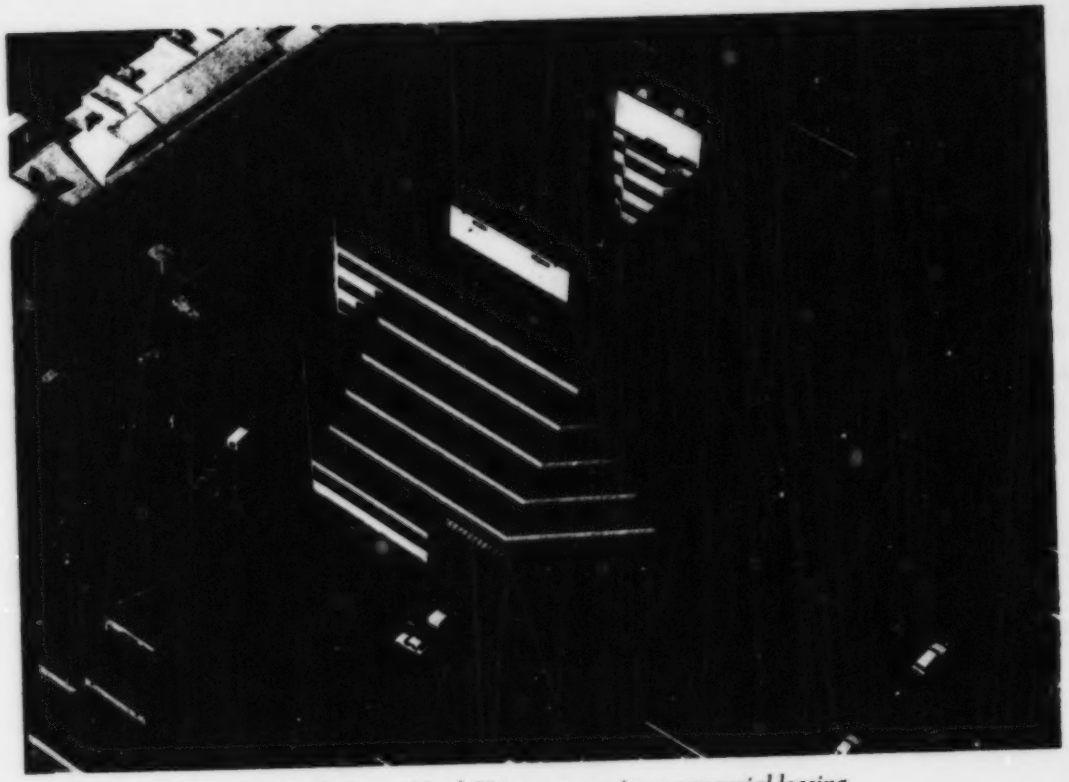
Formation of BC Rail's Real Estate Development business unit followed the financial reorganization of British Columbia Railway Company in 1984. Among other responsibilities, the unit manages 23,700 acres of land owned by the operating railway company, BC Rail Ltd., which is used primarily for rights-of-way, sidings, terminals, station grounds and other railway purposes.

Another effect of the restructuring was the creation of a subsidiary company, BCR Properties Ltd. which, as well as holding title to other land surplus to operating requirements, is also a majority shareholder in the operating railway itself, BC Rail Ltd.

The Real Estate Development unit provides land development and management services to both BC Rail Ltd. and BCR Properties Ltd. Its objectives are to optimize revenues and long-term profitability of both BC Rail and BCR Properties, maximize real estate values and provide support to BC Rail Ltd. in such matters as land acquisitions, legal surveys and industrial trackage agreements. It contributes to group profitability through lease revenues, land sales, timber and gravel royalties and industrial and commercial development projects.

In 1990, the unit completed a number of land acquisitions on behalf of BC Rail Ltd., in which title was acquired for lands needed for bank-widening, grade stabilization and other right-of-way uses. Railway land acquisitions are made by application for Crown grant where such lands are government-owned. In the case of privately-owned lands, acquisition is by negotiation with the owners.

Land leasing is a major source of revenue for the Real Estate business unit. Development of a continuing resource management program, currently in progress, will ensure that timber and gravel royalties are maximized and enhance the unit's contribution to overall revenues. The Real Estate business unit is also responsible for commercial leasing in the group's North Vancouver headquarters building, BC Rail Centre. Officially opened and occupied in 1983, the Centre offers approximately 34,000 square feet of leasable space, most of which is currently occupied. The business unit markets vacant space both directly and through licensed realtors.



BC Rail Centre, North Vancouver—prime commercial leasing.

In order to identify, as far as possible, land requirements over the next 30 years, Real Estate Development has undertaken a strategic land review. The land requirements determined will be compared with the group's current land inventory to identify shortfalls and surpluses community by community. The unit also actively monitors local real estate markets and economic developments throughout the province.

Since it was formed in 1984, the Real Estate unit has actively promoted and marketed its range of landholdings and within the framework of a developing corporate strategic plan will be placing an increasing emphasis on commercial and industrial properties generating an income stream for the future.

INTERMODAL SERVICES

BC Rail has been carrying trailers on flat cars (TOFC) for more than 30 years—but its involvement in carrying and distributing "less than trailer load" (LTL) freight in B.C. dates back almost to the beginning of the railway.

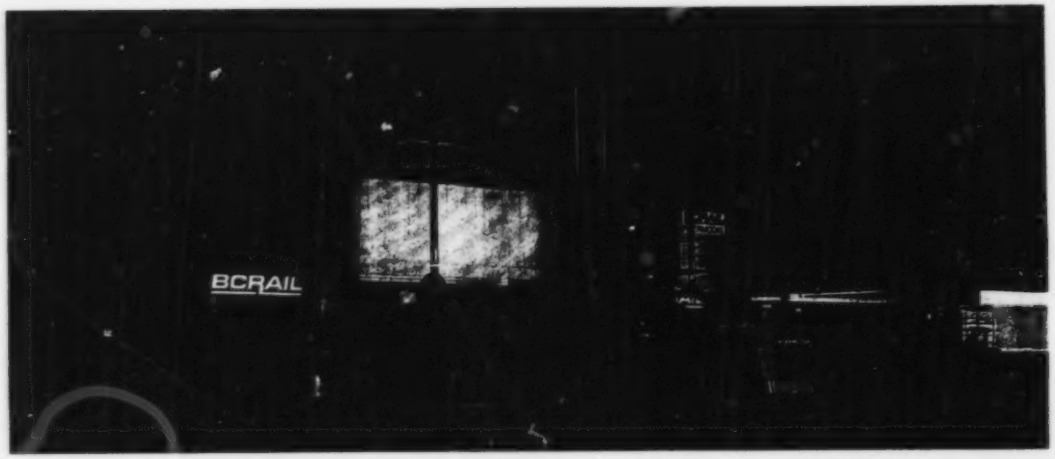
In recognition of a growing need for an integrated provincial transportation system, the railway's former Intermodal department was reorganized early in 1982 to become a new, separately reporting Intermodal Services business unit. In conjunction with the railway's mainline freight operation, the unit offers a variety of transportation options to nearly two-thirds of the province, including LTL, TOFC or "piggyback" service, highway haulage, forest products handling and the distribution and carriage of bulk commodities.

Intermodal's main areas of operations are in southwestern British Columbia and adjacent to the railway's main line as far north as Fort Nelson—nearly 1,000 miles away—and points west of Prince George to Prince Rupert, on B.C.'s north coast.

The unit has operating freight handling warehouses in North Vancouver, Prince George, Williams Lake and Quesnel, all of which—as well as Chetwynd and Fort St. John—are served daily. Fort Nelson is served three times a week.

Intermodal Services operated a fleet of 35 tractors, nine conventional trucks and 390 trailers in 1990. Some of these will be replaced in 1991 by 10 new, 45-foot flatdeck trailers. Forty and 45-foot flatdeck trailers are the mainstay of the intermodal fleet. They are commonly used for transporting building materials, structural steel, pipe and a variety of equipment and machinery, while a number of expandable "trombone" trailers accommodate overlength loads.

As well as high and lowbed flatdecks,



Intermodal's 90,000-pound trailer lifter in new North Vancouver facility.

Intermodal also operates a large number of dry van trailers, as well as heated and refrigerated units for carrying perishables. This equipment ranges from 45 to 53 feet in length. Its own fleet aside, Intermodal Services also offers a transportation service for customers' own trailers with a variety of service permutations for local cartage to and from rail ramp locations.

In 1990, the railway's intermodal area in North Vancouver was completely rebuilt and modernized. Until the new facility opened in mid-year, TOFC loading had involved driving trailers on and off trains, a process known as "circus" loading. Circus loading has now been replaced with a 90,000-pound capacity trailer-lifter which, along with new and relocated trackage in the intermodal area, offers more efficient sideloading of trailers on to trains.

The new facility also includes a lumber reload shed, which provides a covered area for the efficient transfer of forest products from rail to road equipment; new fuelling facilities and pavement of the entire intermodal service area.

BC Rail is also upgrading its intermodal railcar fleet in the coming year with the addition of 15 three-platform articulated cars for handling trailers and containers. This railcar configuration was developed for specific BC Rail Intermodal requirements and is the first of its kind in North America.

Northbound intermodal traffic originates mainly in southwestern B.C. and primarily consists of foodstuffs, liquor, beer, construction materials and chemicals. Southbound traffic mainly comprises forest products of all kinds, beer and scrap metal, which largely originate in on-line points served by the railway.

The unit is actively seeking new markets and has developed market-based pricing policies designed to attract new sources of traffic while improving the economic contribution to the business unit. A review by an independent consulting firm has confirmed that the Intermodal operation generates a positive contribution to the railway's overall profitability.

Trailer on flat car transportation is both fuel and manpower efficient. It combines the speed of road transportation with the economies of rail and is proving to be an attractive alternative to line haulage by road.

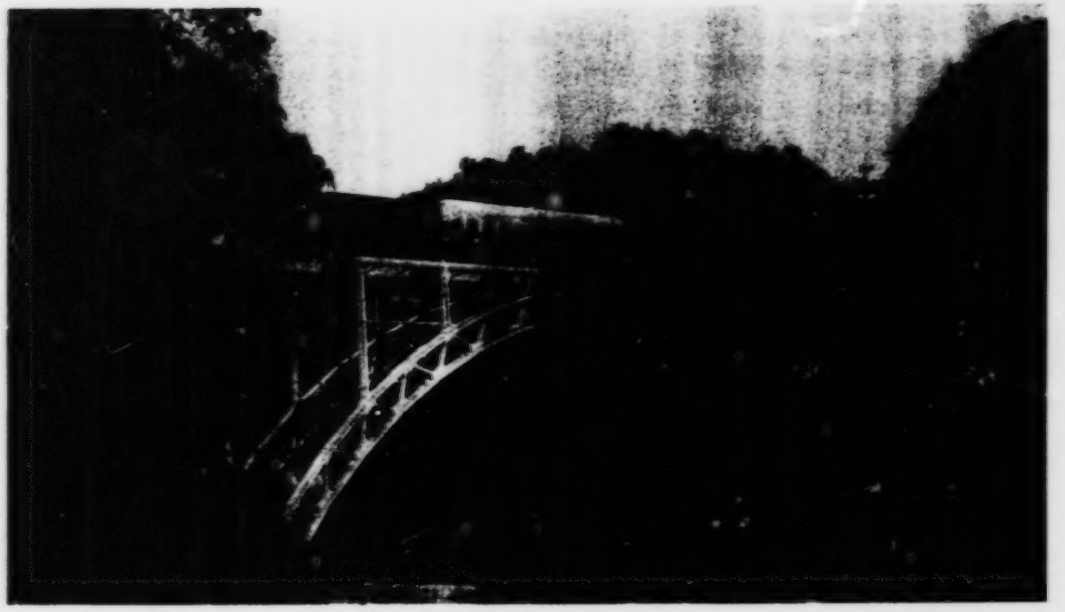
INTERNATIONAL RAIL CONSULTANTS

International Rail Consultants (IRC) was established in 1985 as a joint venture with Sandwell Inc., to provide railway consulting services to industries and governments worldwide. Since that time, IRC's expert staff of civil, electrical and mechanical engineers, economists, planners and other specialists have completed a number of important projects in many overseas countries. The joint venture combines the internationally-recognized transportation consulting experience of Sandwell with the day-to-day operating knowledge of BC Rail.

The two companies have extensive experience in all aspects of railway planning, management, economics, engineering, operations, electrification and telecommunications. To meet the needs of its growing list of clients, IRC draws from the resources of both companies. Principal areas of IRC expertise are in railway electrification; plant design and maintenance; telecommunications; capacity and network analysis; railway management information systems; rolling stock procurement; rebuild and maintenance and general management.

The company also offers a full range of structural, mechanical, industrial and electrical engineering capability, as well as construction and project management skills. It also maintains working associations with educational institutions and training consulting organizations.

In the six years since it was founded, IRC has provided technical assistance to Bangladesh Railways, aimed at increasing motive power availability through improved maintenance practices. The company was also involved in the conceptual design of the Ombilin coalmine development and transportation project in West Sumatra, Indonesia.



Indonesia's Ombilin line, West Sumatra.

In southern Africa, IRC has assisted in telecommunications and signals studies; regional transport operations planning; coal transport and railway support studies; motive power and rolling stock planning and a variety of other consulting engagements throughout the region.

Some of the other countries in which contracts have been undertaken include Colombia, Venezuela, Cameroun, Mozambique and Australia. In Mozambique, IRC took part in a study to examine the feasibility of reopening the 333-mile Limpopo railway line, closed as a result of civil war. Elsewhere in the country, a second study to determine the optimal use of other lines was completed, using a series of computer models for economic analysis.

BC Rail's leadership and expertise in electrified coal transportation played a major role in costing and developing a coal carrying railway in northwestern Venezuela. The work included development of the complete operating system, motive power and rolling stock considerations, track maintenance and human resource counselling.

A coal transportation study in northern Colombia involved analyzing the capacity of an existing railway line and operational system to haul more than 10 million tons of coal annually. The project included inspections of trackage, bridges and other plant, together with the development of spur line costs and locations.

BC Rail's electrified coal-carrying line in northeastern British Columbia helped pioneer 50 kilovolt rail technology. When the line opened in 1984, it was one of only three 50 kv railways in the world and in the intervening years, it has proven to be a clean, quiet and fuel-efficient means of heavy-freight transportation. The engineering and operating knowledge gained from the line—the first electrified freight railway in Canada—is available through IRC.

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British Columbia Railway Company
Consolidated Financial Statements

British Columbia Railway Company
Report of Management

The accompanying consolidated financial statements of British Columbia Railway Company and all other information contained in the Annual Report are the responsibility of management. The consolidated financial statements were prepared in conformity with generally accepted accounting principles appropriate in the circumstances in a manner consistent with the previous year and, accordingly include some amounts based on management's best judgements and estimates. The financial information contained elsewhere in this Annual Report is consistent with that in the consolidated financial statements.

Management is responsible for maintaining a system of internal accounting controls and procedures to provide reasonable assurance, at an appropriate cost/benefit relationship, that assets are safeguarded and that transactions are authorized, recorded and reported properly. The internal accounting control system is augmented by a program of internal audits and appropriate reviews by management, written policies and guidelines and a written Code of Business Conduct adopted by the Board of Directors, applicable to all employees of the company. Management believes that the company's internal accounting controls provide reasonable assurance that assets are safeguarded against material loss from unauthorized use or disposition and that the financial records are reliable for preparing financial statements and other data and maintaining accountability for assets.

The Audit and Finance Committee of the Board of Directors, composed solely of directors who are not officers of the company, meets with the independent auditors, management and internal auditors periodically to discuss internal accounting controls, auditing and financial reporting matters. The committee reviews with the independent auditors the scope and results of the audit effort. The committee also meets with the independent auditors without management present to ensure that the independent auditors have free access to the committee. The committee reviews the consolidated annual financial statements and recommends their approval by the Board of Directors.

The independent auditors, Coopers & Lybrand, are appointed by the Lieutenant Governor in Council to examine the financial statements of British Columbia Railway Company and conduct such tests and related procedures as they deem necessary in conformity with generally accepted auditing standards. The opinion of the independent auditors, based upon their examination of the financial statements, is contained in this Annual Report.

P. J. McElligott,
President and
Chief Executive Officer

J. R. Clarke,
Vice-President,
Finance and Information Services

Auditors' Report

To the Lieutenant Governor in Council
Province of British Columbia

We have audited the consolidated balance sheets of British Columbia Railway Company as at December 31, 1990 and 1989 and the consolidated statements of income and retained earnings and cash flow for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at December 31, 1990 and 1989 and the results of its operations and the changes in its cash position for the years then ended in accordance with generally accepted accounting principles.

Coopers & Lybrand

Vancouver, Canada
February 4, 1991

British Columbia Railway Company
Consolidated Income and Retained Earnings

(Dollars in Thousands)

For the years ended December 31	1990	1989
Revenues		
Rail operations	$ 285,464	$ 319,903
Government assistance - Note 9	9,589	9,050
	295,053	328,953
Expenses		
Operations	67,187	67,974
Equipment	63,939	67,644
Road	42,155	45,570
Depreciation	39,423	36,985
General and administration	24,585	23,542
	237,289	241,715
Railway operating income	57,764	87,238
Non-operating income (expense)		
Interest - Note 10	(9,048)	(8,663)
Other income	4,287	4,838
Large Corporations tax	(1,950)	(931)
Income before minority interest and extraordinary item	51,053	82,482
Minority interest	(17,271)	(17,893)
Income before extraordinary item	33,782	64,589
Extraordinary item - Note 2	0	(80,646)
Net income (loss)	33,782	(16,057)
Retained earnings, beginning of year	149,649	176,014
	183,431	159,957
Dividends paid	(10,308)	(10,308)
Retained earnings, end of year	$ 173,123	$ 149,649

On behalf of the Board

Director

Director

British Columbia Railway Company
Consolidated Balance Sheets

(Dollars in Thousands)

December 31	1990	1989
Assets		
Current assets		
Cash and short-term investments	$ (1,598)	$ 44,787
Accounts receivable	34,834	40,003
Material and other items	39,844	38,553
	73,080	123,343
Property and equipment		
Road and buildings	1,297,195	1,247,501
Equipment	325,165	284,539
	1,622,360	1,532,040
Accumulated depreciation	365,924	339,037
	1,256,436	1,193,003
	$ 1,329,516	$ 1,316,346
Liabilities and Shareholder's Equity		
Current liabilities		
Accounts payable	$ 89,675	$ 100,218
Current obligations on long-term debt	29,867	26,954
	119,542	127,172
Long-term debt - Note 3	81,946	84,235
Minority interest - Note 4	186,501	186,886
Shareholder's equity		
Share capital - Note 5	257,688	257,688
Contributed surplus	510,716	510,716
Retained earnings	173,123	149,649
	941,527	918,053
Commitments - Note 6		
Contingent liabilities - Note 7		
	$ 1,329,516	$ 1,316,346

British Columbia Railway Company
Consolidated Cash Flow

(Dollars in Thousands)

For the years ended December 31	1990	1989
Operating activities		
Income before extraordinary item	**$ 33,782**	$ 64,589
Add (deduct)		
Item not affecting working capital		
Depreciation	**39,423**	36,985
Net changes in non-cash working capital		
Accounts receivable	**5,169**	(1,562)
Material and other items	**(1,291)**	(4,806)
Accounts payable	**(10,910)**	20,043
Minority interest in earnings	**17,271**	17,893
Interest	**9,048**	8,663
	92,492	141,805
Investing activities		
Additions to property and equipment	**(106,118)**	(71,561)
Change in payables for equipment purchases	**367**	(252)
Government assistance for capital items	**3,262**	4,117
	(102,489)	(67,696)
Financing activities		
Issue of long-term debt	**27,695**	0
Repayment of long-term debt	**(27,071)**	(2,037)
Interest	**(9,048)**	(8,663)
Dividends paid to minority interest	**(17,271)**	(17,893)
Reduction in minority interest	**(385)**	(13,114)
	(26,080)	(41,707)
Dividends paid	**(10,308)**	(10,308)
Increase (decrease) in cash	**(46,385)**	22,094
Cash and short-term investments, beginning of year	**44,787**	22,693
Cash and short-term investments, end of year	**$ (1,598)**	$ 44,787

British Columbia Railway Company
Notes to Consolidated Financial Statements

1. SIGNIFICANT ACCOUNTING POLICIES

The accounting regulations prescribed by the National Transportation Agency of Canada have been adopted to the extent that this is possible without submitting specific accounting policies and depreciation rates to the Agency for approval.

Basis of consolidation

The consolidated financial statements include the accounts of British Columbia Railway Company and its subsidiaries, BC Rail Ltd. and BCR Properties Ltd. In these notes "company" refers to British Columbia Railway Company and its subsidiaries. All significant inter-company transactions are eliminated.

Class of business

The company provides a fully integrated rail freight service within British Columbia. Services other than hauling freight are not of sufficient size to warrant separate reporting.

Road property

New construction is recorded at cost net of Government grants. Abandoned or relocated sections are removed at average unit costs. Elements of track structure installed during planned programs are recorded at cost and the material replaced is removed at amounts which approximate average unit costs. Labour costs for programmed replacements are expensed as incurred.

Depreciation

Depreciation is provided for major categories of property and equipment on the straight-line basis at composite rates estimated to reduce the original cost to estimated salvage value over the average service lives of the classes. The group method is used for recording depreciation under which, on disposal, the original cost of assets retired less salvage value is charged against accumulated depreciation. No gain or loss on retirements, other than on accidental destruction of rolling stock and on disposal of land, is included in income. The original cost of assets less estimated salvage value is depreciated over the following number of years:

	Number of Years
Grade and tunnels	100
Rail	35
Ties	15-35
Ballast	25
Bridges	30-80
Locomotives and power units	25
Freight cars	15-33

Repairs

Repairs and non-programmed replacements of track structure are charged against current operations. Betterments and major track relocations are capitalized.

Material and supplies

Inventories of material and supplies are valued at the lower of average cost and net realizable value.

Government assistance

Grants directly related to the construction or rehabilitation of road property have offset related road property capital expenditures. Operating assistance has been deducted from the related expense accounts or included in revenue.

Income taxes

Income tax expense is computed on the basis of accounting income recorded by BC Rail Ltd. The income of British Columbia Railway Company and BCR Properties Ltd. is exempt from income taxes.

Transactions in foreign currency

Transactions originating in foreign currency are translated at the approximate exchange rates prevailing at the dates of the transactions. Assets and liabilities denominated in foreign currency at the balance sheet date are translated to equivalent Canadian amounts at the current rate of exchange.

Leases

Certain long-term lease transactions relating to the financing of equipment are accounted for as purchases. The capital lease obligations reflect the present value of future minimum rental payments discounted at the interest rate implicit in the leases. The capitalized values of depreciable assets are generally depreciated over the related lease terms in equal annual amounts. Costs of all other leases are charged against operations as incurred.

2. EXTRAORDINARY ITEM

During 1989, construction costs of $80.6 million relating to the northernmost 340 kilometres of the incomplete Dease Lake extension were determined to have no future economic benefit to the company and were written off.

3. LONG-TERM DEBT

Long-term debt outstanding, less current maturities, consists of the following (in thousands):

	1990	1989
Sinking fund bonds and debentures payable to the Province of British Columbia (the Province)		
11.00%, due June 1995	**$ 25,000**	$ 25,000
10.99%, due August 2005	**24,490**	24,490
	49,490	49,490
Less sinking fund	**1,244**	935
	48,246	48,555
Bond payable to the Province		
10.75%, due February 1990	**0**	25,000
Capital lease obligations - Notes 6 and 12	**35,872**	37,634
Short-term notes payable to the Province	**27,695**	0
	111,813	111,189
Deduct current portion	**29,867**	26,954
	$ 81,946	$ 84,235

4. MINORITY INTEREST

The minority interest consists of 7,460,045 (1989 - 7,475,445) series 1-A first preferred shares with a par value of $25 each issued by BC Rail Ltd. These shares are designated as $2.3125 cumulative, redeemable and retractable. The retraction privilege has expired.

BC Rail Ltd. must make all reasonable efforts in each quarter to purchase for cancellation on the open market three-quarters of 1% of the series 1-A preferred shares outstanding at the beginning of the quarter at a price not to exceed $25 per share and all transaction costs. If it is unable to fulfill its obligation in any calendar quarter the obligation will carry over only to the successive calendar quarters of the same calendar year and will thereafter be extinguished. During the year, 15,400 shares were purchased on the open market and subsequently cancelled. During 1989, pursuant to retraction rights then in effect, BC Rail Ltd. acquired 524,555 shares at $25 each.

5. SHARE CAPITAL

Authorized:

10,000,000 shares with a par value of $100 each.

Issued and outstanding:

2,576,885 shares held by the Province.

As all of the shares are held by the Province, earnings per share have not been provided.

6. COMMITMENTS

The company has significant lease commitments for rolling stock and additional minor lease commitments for equipment and real estate which expire at various dates prior to the year 2003. Certain of these leases transfer substantially all of the benefits and risks of ownership to the company and are accounted for as capital leases.

The following is a schedule of future minimum rental payments at December 31, 1990 required under non-cancellable leases that have remaining terms in excess of one year (in thousands):

	Capital Leases	Operating Leases
1991	$ 6,789	$ 13,935
1992	6,789	12,690
1993	6,789	10,576
1994	6,789	6,691
1995	6,789	5,989
Later years	30,803	15,871
Total minimum lease payments	64,748	$ 65,752
Less		
Executory costs	5,082	
Imputed interest	23,794	
Present value	$ 35,872	

Assets under capital leases recorded in the property and equipment accounts as at December 31, with effective interest rates in the range of 11.75% to 12.02% are as follows (in thousands):

	1990	1989
Equipment	$ 46,283	$ 46,283
Accumulated depreciation	19,363	17,502
	$ 26,920	$ 28,781

As at December 31, 1990 the company had outstanding purchase commitments for the acquisition of material and equipment amounting to $8 million.

7. CONTINGENT LIABILITIES

The company is contingently liable with respect to pending litigation and claims arising in connection with rail line construction and in the normal course of business. In the opinion of management, any liability that may arise will be capitalized or would not have a material adverse effect on future income.

8. INCOME TAX

At December 31, 1990, BC Rail Ltd. had approximately $107 million excess income tax value over net book value of depreciable property and equipment which can be used to reduce future years' earnings for income tax purposes. The effect of such benefits, approximating $48 million, will be recognized in the accounts in the future as they are realized.

9. GOVERNMENT ASSISTANCE

Government assistance was as follows (in thousands):

	1990	1989
Unapplied, beginning of year	$ 518	$ 0
Contributions during the year		
From the Province		
Fort Nelson extension		
Operating	6,250	4,787
Rehabilitation	5,575	7,198
Passenger operations	3,887	2,868
Passenger car modernization	278	482
	15,990	15,335
From the Government of Canada		
Grain transportation	1,277	1,395
	17,267	16,730
Total available	17,785	16,730
Applied as follows		
Revenue		
Fort Nelson extension	5,000	4,787
Passenger operations	3,312	2,868
Grain transportation	1,277	1,395
	9,589	9,050
Operating expenses		
Fort Nelson extension	1,290	2,714
Passenger operations	778	331
	2,068	3,045
Property and equipment	3,262	4,117
Total applied	14,919	16,212
Unapplied, end of year	$ 2,866	$ 518

10. INTEREST EXPENSE

Interest expense was as follows (in thousands):

	1990	1989
Interest on long-term debt and notes to the Province	$ 7,786	$ 8,123
Interest on capital lease obligations	4,387	4,631
	12,173	12,754
Less		
Sinking fund earnings	119	89
Interest earned on temporary investments	3,006	4,002
	3,125	4,091
Net interest	$ 9,048	$ 8,663

11. PENSION PLAN AND POSTEMPLOYMENT BENEFITS

The company maintains a contributory defined benefit plan which covers substantially all of its employees. The plan provides pensions based on length of service and average earnings.

An actuarial valuation of the plan as at July 31, 1990 indicates that the accrued pension obligations and the net assets available to provide for these obligations are as follows:

Accrued pension obligations	$197 million
Pension fund assets	$222 million

To reduce the excess of pension fund assets over the accrued pension obligations, a contribution holiday was implemented from March, 1989 to March, 1991.

The company also provides basic medical insurance coverage for all retired employees. The cost of the premiums is charged to income as they are paid.

12. RELATED PARTY TRANSACTIONS

Related party information not presented elsewhere in the notes to financial statements is presented below.

First preferred shares of BC Rail Ltd. and certain capital lease obligations are guaranteed by the Province. The Ministry of Finance and Corporate Relations of the Province acts as fiscal agent and the Superannuation Commission of the Province administers the company pension plan. Fees are charged for both of these services.

Except for income tax as described in Note 1, the company is subject to all taxes levied by the Province except most property taxes. All other transactions between the company and the Province are at terms no more or less favourable than those with unrelated parties.

British Columbia Railway Company
Five-Year Review
Consolidated Statement
(Dollars in Thousands)

	FISCAL YEAR				
	1990	1989	1988	1987	1986
Revenues					
Rail operations	**$ 285,464**	$ 319,903	$ 319,710	$ 315,707	$ 308,659
Government assistance	**9,589**	9,050	7,284	9,890	9,151
	295,053	328,953	326,994	325,597	317,810
Expenses					
Operations	**67,187**	67,974	70,674	71,216	67,928
Equipment	**63,939**	67,644	66,580	67,042	69,171
Road	**42,155**	45,570	45,516	48,117	43,274
Depreciation	**39,423**	36,985	35,853	34,870	32,359
General and administration	**24,585**	23,542	24,086	23,542	24,046
	237,289	241,715	242,709	244,787	236,778
Railway operating income	**57,764**	87,238	84,285	80,810	81,032
Non-operating income (expense)					
Interest	**(9,048)**	(8,663)	(11,145)	(11,839)	(13,687)
Other income	**4,287**	4,838	3,676	3,267	4,730
Large Corporations tax	**(1,950)**	(931)	0	0	0
Income before deferred income taxes	**51,053**	82,482	76,816	72,238	72,075
Provision for (recovery of) deferred income taxes	**0**	0	0	(517)	2,138
Income before minority interest and extraordinary item	**51,053**	82,482	76,816	72,755	69,937
Minority interest	**(17,271)**	(17,893)	(18,500)	(18,500)	(18,500)
Income before extraordinary item	**33,782**	64,589	58,316	54,255	51,437
Extraordinary item	**0**	80,646	0	0	0
Net income (loss)	**$ 33,782**	$ (16,057)	$ 58,316	$ 54,255	$ 51,437
CARLOADINGS					
Total revenue cars loaded on line	**197,643**	215,651	222,762	229,506	232,367
Received from connections	**2,101**	2,991	3,209	3,656	3,330
Total carloadings	**199,744**	218,642	225,971	233,162	235,697
MOTIVE POWER—Electric	**7**	7	7	7	7
—Diesel	**114**	114	116	117	109
ROLLING STOCK—Freight	**9,958**	9,914	9,908	10,107	10,146
—Passenger	**9**	9	9	9	9
—Boarding and work	**472**	505	469	449	455
TONS HAULED	**15,851,000**	16,955,000	17,340,000	17,670,000	17,854,000
EMPLOYEES AT YEAR END	**2,480**	2,700	2,700	2,760	2,660

British Columbia Railway Company Financial Review

Consolidated net income for 1990 was $33.8 million compared with 1989 consolidated income of $64.6 million, before an extraordinary item of $80.6 million. The reduction of $30.8 million, or 48%, is the result of a decline in rail freight revenues and a month long labour dispute.

Revenues

Due to onset of a recession both in Canada and the United States during 1990 and abnormal operating conditions which resulted in 66 days of mainline closures in the last half of the year, freight revenues deteriorated 11% from 1989 levels. The reduction in carloadings had a corresponding negative impact on the revenue in rental from equipment and switching.

Expenses

Consolidated operating expenses decreased by $4.4 million (2%) to $237.3 million for 1990.

The average price of fuel increased by 11% from 1989, however lower consumption resulting from the decline in freight traffic more than offset the price increase.

Total labour costs declined by $4.8 million from the 1989 level. This reduction was mainly due to a one month labour dispute and reductions in staffing levels. These reductions were partially offset by wage increases resulting from the renewal of the collective agreements with the unionized employees and severance settlements for terminated employees.

Equipment maintenance costs were reduced through the purchase of new locomotives. Further cost reductions were achieved in various operating expenses through the deferral of discretionary maintenance programs.

Depreciation costs increased $2.4 million (7%) over 1989 levels, the result of continued upgrading of the company's equipment and physical plant.

Operating Ratio

The company's operating ratio, the ratio of operating expenses, including depreciation, to revenue, deteriorated in 1990 to .80 (1989-.73).

Non-Operating Items

Due to reduced short term investments net interest expense increased during 1990 by $0.4 million (4%) to $9 million.

The Large Corporations tax for 1990 increased $1 million to $1.9 million. The tax was effective for a full year in 1990 compared to only six months in 1989.

Minority Interest

The minority interest on the consolidated income statement reflects the payment of dividends by the operating subsidiary, BC Rail Ltd., to holders of its series 1-A preferred shares. Due to the retraction and repurchases of shares in 1989 and 1990, dividend payments declined by $0.6 million.

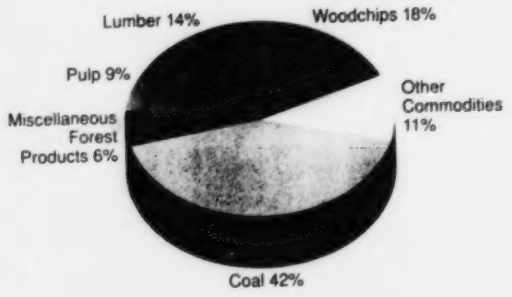
Dividends Paid

In 1990, British Columbia Railway Company paid its shareholder, the Province of British Columbia, a dividend of $10.3 million on its common shares. This is the fifth successive year that a dividend of this amount has been paid.

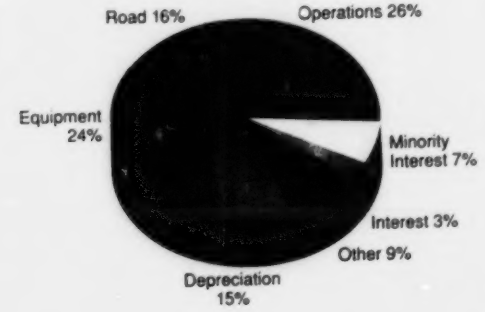
Additional Comments

Substantially all of the group's operations are conducted by BC Rail Ltd., for which additional discussion and analysis is provided.

Revenue Tons by Commodity



Consolidated Expenses



DF
Dairyland
Foods
CANADI
KILN DRIED
KILN DRIED
LIVINGSTON
FINLAY
FOREST
INDUSTRIES LTD.

Garibaldi Building Supplies Ltd.
PAINT • LUMBER • PLYWOOD
HARDWARE • PANELING • PLUMBING • LOTS MORE
SEABOARD
INTERNATIONAL TERMINAL
DIVISION OF SEABOARD SHIPPING COMPANY LIMITED
SLOCAN GROUP

BC Rail Ltd.
Financial Statements

BC Rail Ltd.
Report of Management

The accompanying financial statements of BC Rail Ltd. and all other information contained in the Annual Report are the responsibility of management. The financial statements were prepared in conformity with generally accepted accounting principles appropriate in the circumstances in a manner consistent with the previous year and, accordingly include some amounts based on management's best judgements and estimates. The financial information contained elsewhere in this Annual Report is consistent with that in the financial statements.

Management is responsible for maintaining a system of internal accounting controls and procedures to provide reasonable assurance, at an appropriate cost/benefit relationship, that assets are safeguarded and that transactions are authorized, recorded and reported properly. The internal accounting control system is augmented by a program of internal audits and appropriate reviews by management, written policies and guidelines and a written Code of Business Conduct adopted by the Board of Directors, applicable to all employees of the company. Management believes that the company's internal accounting controls provide reasonable assurance that assets are safeguarded against material loss from unauthorized use or disposition and that the financial records are reliable for preparing financial statements and other data and maintaining accountability for assets.

The Audit and Finance Committee of the Board of Directors, composed solely of directors who are not officers of the company, meets with the independent auditors, management and internal auditors periodically to discuss internal accounting controls, auditing and financial reporting matters. The committee reviews with the independent auditors the scope and results of the audit effort. The committee also meets with the independent auditors without management present to ensure that the independent auditors have free access to the committee. The committee reviews the annual financial statements and recommends their approval by the Board of Directors.

The independent auditors, Coopers & Lybrand, are appointed by the shareholders to examine the financial statements of BC Rail Ltd. and conduct such tests and related procedures as they deem necessary in conformity with generally accepted auditing standards. The opinion of the independent auditors, based upon their examination of the financial statements, is contained in this Annual Report.

P. J. McElligott,
President and
Chief Executive Officer

J. R. Clarke,
Vice-President,
Finance and Information Services

Auditors' Report

To the Shareholders

We have audited the balance sheets of BC Rail Ltd. as at December 31, 1990 and 1989 and the statements of loss and deficit, contributed surplus and cash flow for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the company as at December 31, 1990 and 1989 and the results of its operations and the changes in its cash position for the years then ended in accordance with generally accepted accounting principles. As required by the British Columbia Company Act, we report that, in our opinion, these principles have been applied on a consistent basis.

Coopers & Lybrand

Vancouver, Canada
February 4, 1991

BC Rail Ltd.
Loss and Deficit
(Dollars in Thousands)

For the years ended December 31	1990	1989
Revenues		
Rail operations	**$ 285,464**	$ 319,903
Government assistance - Note 8	**9,589**	9,050
	295,053	328,953
Expenses		
Operations	**67,187**	67,974
Equipment	**63,939**	67,644
Road	**42,175**	45,570
Depreciation	**39,423**	36,985
General and administration	**24,525**	23,542
	237,249	241,715
Railway operating income	**57,804**	87,238
Non-operating income (expense)		
Interest - Note 9	**(85,666)**	(85,316)
Other income	**2,118**	1,898
Large Corporations tax	**(1,950)**	(931)
Income (loss) before extraordinary item	**(27,694)**	2,889
Extraordinary item - Note 2	**0**	(80,646)
Net loss	**(27,694)**	(77,757)
Deficit, beginning of year	**(82,706)**	(4,949)
Deficit, end of year	**$ (110,400)**	$ (82,706)

On behalf of the Board

Director *Director*

BC Rail Ltd.
Balance Sheets
(Dollars in Thousands)

December 31	1990	1989
Assets		
Current assets		
Cash and short-term investments	**$ (1,598)**	$ 44,787
Accounts receivable	**34,834**	40,003
Material and other items	**39,527**	38,530
	72,763	123,320
Property and equipment		
Road and buildings	**1,290,910**	1,242,270
Equipment	**325,165**	284,539
	1,616,075	1,526,809
Accumulated depreciation	**365,924**	339,037
	1,250,151	1,187,772
	$ 1,322,914	$ 1,311,092
Liabilities and Shareholders' Equity		
Current liabilities		
Accounts payable	**$ 88,525**	$ 97,997
Current obligations on long-term debt	**104,436**	67,007
Due to related companies	**109,214**	87,286
	302,175	252,290
Long-term debt - Note 3	**619,461**	610,170
Shareholders' equity		
Share capital - Note 4	**399,191**	399,576
Contributed surplus	**112,487**	131,762
Deficit	**(110,400)**	(82,706)
	401,278	448,632
Commitments - Note 5		
Contingent liabilities - Note 6		
	$ 1,322,914	$ 1,311,092

BC Rail Ltd.
Contributed Surplus
(Dollars in Thousands)

December 31	1990	1989
Balance, beginning of year	$ 131,762	$ 51,655
Contributed on issue of shares	0	100,000
Loss on redemption of shares	(4)	0
	131,758	151,655
Dividends paid		
Preferred shares	17,271	17,893
Common shares	2,000	2,000
	19,271	19,893
Balance, end of year	$ 112,487	$ 131,762

BC Rail Ltd.
Cash Flow
(Dollars in Thousands)

For the years ended December 31	1990	1989
Operating activities		
Income (loss) before extraordinary item	$ (27,694)	$ 2,889
Add (deduct)		
Item not affecting working capital		
Depreciation	39,423	36,985
Net changes in non-cash working capital		
Accounts receivable	5,169	(2,493)
Material and other items	(997)	(4,807)
Accounts payable	(9,839)	20,981
Related company accounts	21,928	30,391
Interest	85,666	85,316
	113,656	169,262
Investing activities		
Additions to property and equipment	(105,064)	(71,199)
Change in payables for equipment purchases	367	(252)
Government assistance for capital items	3,262	4,117
	(101,435)	(67,334)
Financing activities		
Issue of long-term debt	73,482	40,245
Repayment of long-term debt	(26,762)	(102,756)
Interest	(85,666)	(85,316)
Issue of preferred shares	0	101,000
Redemption of preferred shares	(385)	(13,114)
Loss on redemption of shares	(4)	0
	(39,335)	(59,941)
Dividends paid	(19,271)	(19,893)
Increase (decrease) in cash	(46,385)	22,094
Cash and short-term investments, beginning of year	44,787	22,693
Cash and short-term investments, end of year	$ (1,598)	$ 44,787

BC Rail Ltd.
Notes to Financial Statements

1. SIGNIFICANT ACCOUNTING POLICIES

The accounting regulations prescribed by the National Transportation Agency of Canada have been adopted to the extent that this is possible without submitting specific accounting policies and depreciation rates to the Agency for approval.

Class of business

The company provides a fully integrated rail freight service within British Columbia. Services other than hauling freight are not of sufficient size to warrant separate reporting.

Road property

New construction is recorded at cost net of Government grants. Abandoned or relocated sections are removed at average unit costs. Elements of track structure installed during planned programs are recorded at cost and the material replaced is removed at amounts which approximate average unit costs. Labour costs for programmed replacements are expensed as incurred.

Depreciation

Depreciation is provided for major categories of property and equipment on the straight-line basis at composite rates estimated to reduce the original cost to estimated salvage value over the average service lives of the classes. The group method is used for recording depreciation under which, on disposal, the original cost of assets retired less salvage value is charged against accumulated depreciation. No gain or loss on retirements, other than on accidental destruction of rolling stock and on disposal of land, is included in income. The original cost of assets less estimated salvage value is depreciated over the following number of years:

	Number of Years
	100
Grade and tunnels	35
Rail	15-35
Ties	25
Ballast	30-80
Bridges	25
Locomotives and power units	15-33
Freight cars	

Repairs

Repairs and non-programmed replacements of track structure are charged against current operations. Betterments and major track relocations are capitalized.

Material and supplies

Inventories of material and supplies are valued at the lower of average cost and net realizable value.

Government assistance

Grants directly related to the construction or rehabilitation of road property have offset related road property capital expenditures. Operating assistance has been deducted from the related expense accounts or included in revenue.

Income taxes

Income tax expense is computed on the basis of accounting income recorded by the company.

Transactions in foreign currency

Transactions originating in foreign currency are translated at the approximate exchange rates prevailing at the dates of the transactions. Assets and liabilities denominated in foreign currency at the balance sheet date are translated to equivalent Canadian amounts at the current rate of exchange.

Leases

Certain long-term lease transactions relating to the financing of equipment are accounted for as purchases. The capital lease obligations reflect the present value of future minimum rental payments discounted at the interest rate implicit in the leases. The capitalized values of depreciable assets are generally depreciated over the related lease terms in equal annual amounts. Costs of all other leases are charged against operations as incurred.

2. EXTRAORDINARY ITEM

During 1989, construction costs of $80.6 million relating to the northernmost 340 kilometers of the incomplete Dease Lake extension were determined to have no future economic benefit to the company and were written off.

Long-term debt outstanding, less current maturities, consists of the following (in thousands):

	1990	1989
Capital lease obligations - Notes 5 & 11	$ 35,872	$ 37,634
Deduct current portion	1,981	1,762
	33,891	35,872
Notes payable to British Columbia Railway Company		
10.75%, due February 1990	0	25,000
0.00%, due June 1991	40,245	40,245
9.70%, due June 1991	62,210	62,210
9.96%, due June 1992	68,245	68,245
10.34%, due January 1995	73,482	0
10.40%, due June 1995	41,343	41,343
	285,525	237,043
Deduct current portion	102,455	65,245
	183,070	171,798
Note payable to BCR Properties Ltd. 14%, due June 1999	402,500	402,500
	$ 619,461	$ 610,170

4. SHARE CAPITAL

Authorized:

5,000,000 common shares with a par value of $100 each.

20,000,000 first preferred shares with a par value of $25 each of which 8,000,000 are designated as $2.3125 cumulative redeemable retractable first preferred shares, series 1-A. The retraction privilege has expired.

20,000,000 second preferred shares with a par value of $100 each. 3,000,000 have been designated as series 2-A non-cumulative and redeemable. 10,000 have been designated as series 2-B non-cumulative, redeemable and retractable with a dividend rate of 8% and a retraction price of $10,100 per share.

Issued and outstanding ($ in thousands):

Shares	1990	1989
500,012 common	$ 50,001	$ 50,001
7,460,045 series 1-A preferred (1989 - 7,475,445)	186,501	186,886
1,616,892 series 2-A preferred	161,689	161,689
10,000 series 2-B preferred	1,000	1,000
	$ 399,191	$ 399,576

As all of the common shares are held by British Columbia Railway Company and its wholly owned subsidiary, earnings per share have not been provided.

The company must make all reasonable efforts in each quarter to purchase for cancellation on the open market three-quarters of 1% of the series 1-A preferred shares outstanding at the beginning of the quarter at a price not to exceed $25 per share and all transaction costs. If it is unable to fulfill its obligation in any calendar quarter, the obligation will carry over only to the successive calendar quarters of the same calendar year and will thereafter be extinguished. During the year, 15,400 shares were purchased on the open market and subsequently cancelled. During 1989, pursuant to retraction rights then in effect, the company was required to acquire 524,555 shares at $25 each.

Subsequent to December 31, 1990, the company issued to the British Columbia Railway Company and its wholly-owned subsidiary 6,200 second preferred shares with a par value of $100 each, designated as series 2-C non-cumulative, redeemable and retractable, for a total consideration of $62,620,000. The retraction price is $10,100 per share.

5. COMMITMENTS

The company has significant lease commitments for rolling stock and additional minor lease commitments for equipment and real estate which expire at various dates prior to the year 2003. Certain of these leases transfer substantially all of the benefits and risks of ownership to the company and are accounted for as capital leases.

The following is a schedule of future minimum rental payments at December 31, 1990 required under non-cancellable leases that have remaining terms in excess of one year (in thousands):

	Capital Leases	Operating Leases
1991	$ 6,789	$ 13,935
1992	6,789	12,690
1993	6,789	10,576
1994	6,789	6,691
1995	6,789	5,989
Later years	30,803	15,871
Total minimum lease payments	64,748	$ 65,752
Less		
Executory costs	5,082	
Imputed interest	23,794	
Present value	$ 35,872	

Assets under capital leases recorded in the property and equipment accounts as at December 31, with effective interest rates in the range of 11.75% to 12.02% are as follows (in thousands):

	1990	1989
Equipment	$ 46,283	$ 46,283
Accumulated depreciation	19,363	17,502
	$ 26,920	$ 28,781

As at December 31, 1990 the company had outstanding purchase commitments for the acquisition of material and equipment amounting to $8 million.

6. CONTINGENT LIABILITIES

The company is contingently liable with respect to pending litigation and claims arising in connection with rail line construction and in the normal course of business. In the opinion of management, any liability that may arise will be capitalized or would not have a material adverse effect on future income.

7. INCOME TAX

At December 31, 1990, the company had approximately $107 million excess income tax value over net book value of depreciable property and equipment which can be used to reduce future years' earnings for income tax purposes. The effect of such benefits, approximating $48 million, will be recognized in the accounts in the future as they are realized.

8. GOVERNMENT ASSISTANCE

Government assistance was as follows (in thousands):

	1990	1989
Unapplied, beginning of year	$ 518	$ 0
Contributions during the year		
From the Province		
Fort Nelson extension		
Operating	6,250	4,787
Rehabilitation	5,575	7,198
Passenger operations	3,887	2,868
Passenger car modernization	278	482
	15,990	15,335
From the Government of Canada		
Grain transportation	1,277	1,395
	17,267	16,730
Total available	17,785	16,730
Applied as follows		
Revenue		
Fort Nelson extension	5,000	4,787
Passenger operations	3,312	2,868
Grain transportation	1,277	1,395
	9,589	9,050
Operating expenses		
Fort Nelson extension	1,290	2,714
Passenger operations	778	331
	2,068	3,045
Property and equipment	3,262	4,117
Total applied	14,919	16,212
Unapplied, end of year	$ 2,866	$ 518

9. INTEREST EXPENSE

Interest expense was as follows (in thousands):

	1990	1989
Interest on notes payable		
BCR Properties Ltd.	**$ 56,350**	$ 56,350
British Columbia Railway Company	**25,002**	26,716
	81,352	83,066
Interest on capital lease obligations	**4,387**	4,631
Interest to related companies	**2,933**	1,621
	88,672	89,318
Less interest income	**3,006**	4,002
	$ 85,666	$ 85,316

10. PENSION PLAN AND POSTEMPLOYMENT BENEFITS

The company maintains a contributory defined benefit plan which covers substantially all of its employees. The plan provides pensions based on length of service and average earnings.

An actuarial valuation of the plan as at July 31, 1990 indicates that the accrued pension obligations and the net assets available to provide for these obligations are as follows:

Accrued pension obligations	$197 million
Pension fund assets	$222 million

To reduce the excess of pension fund assets over the accrued pension obligations, a contribution holiday was implemented from March, 1989 to March, 1991.

The company also provides basic medical insurance coverage for all retired employees. The cost of the premiums is charged to income as they are paid.

11. RELATED PARTY TRANSACTIONS

Related party information not presented elsewhere in the notes to financial statements is presented below.

All of the outstanding common and second preferred shares of the company are owned as follows:

BCR Properties Ltd. (a wholly owned subsidiary of British Columbia Railway Company)	75%
British Columbia Railway Company	25%

First preferred shares and certain capital lease obligations are guaranteed by the Province. The Ministry of Finance and Corporate Relations of the Province acts as fiscal agent and the Superannuation Commission of the Province administers the company pension plan. Fees are charged for both of these services.

The company is subject to all taxes levied by the Province except most property taxes. All other transactions between the company and the Province are at terms no more or less favourable than those with unrelated parties.

BC Rail Ltd.
Management Discussion & Analysis

BC Rail Ltd. is the railway operating subsidiary of the British Columbia Railway group. The following information is provided to investors in BC Rail Ltd. in accordance with the guidelines established by the Ontario Securities Commission and the Commission des Valeurs Mobilières du Québec.

General

Railway operating income decreased 34% from 1989 to 1990. BC Rail Ltd.'s operating ratio, the ratio of operating expenses, including depreciation to revenue, deteriorated in 1990 to .80 (1989-.73), largely as a result of a 10% decrease in revenue.

The decline in freight revenue during 1990 was the result of a railway labour dispute, the onset of a recession in both Canada and the United States and abnormal operating conditions which resulted in 66 days of mainline closures in the last half of the year.

During 1990, arbitration proceedings were finalized between a northeast coal shipper and a consortium of Japanese buyers in respect of the export price of coal under their contract. As a result of the arbitrated retroactive reduction in coal prices, the coal shipper filed for protection under the Companies Creditors Arrangement Act, (the "C.C.A.A."). Pursuant to the C.C.A.A., the coal shipper advised that its continued viability requires concessions from suppliers including a reduction in the rail charges. In 1990, coal revenue provided 20% of total revenues; therefore any adjustment in rates would have a significant impact on the income of BC Rail Ltd.

Liquidity

Working capital was reduced by $100 million from 1989 to 1990. Current obligations on long-term debts will be funded from operations or refinanced.

Capital Resources

The 1991 capital expenditures are estimated to be $65 million. At December 31, 1990 BC Rail Ltd. had commitments in place for approximately $6 million of the 1991 capital expenditures.

Funds generated from 1991 operations, together with funds provided by its parent, are anticipated to be sufficient to cover capital, operating, and financing costs of the company; however short-term borrowings will be required. Sufficient lines of credit are maintained.

In the event that revenues are less than projected, the company will reduce planned capital expenditures and discretionary maintenance programs such that additional financing is minimized.

Results of Operations

The 2% average annual growth in revenue experienced from 1985 through 1989 was reversed to a 10% decline during 1990. The primary reason for this decline was a significant reduction in the movement of forest products resulting from the recession and the strike of the unionized employees during the month of September. The reduction in freight revenue also had a direct negative impact on revenue generated from the rental of equipment and switching charges.

Competition continued to exert a strong downward pressure on freight rates through 1990 and will continue into the foreseeable future. A shift in woodchip traffic patterns resulted in a reduction of total freight revenue due to the shorter hauls. The traffic from additional customer sites in 1990 was insufficient to offset revenue reductions.

Operating expenses decreased by 2% in 1990 despite fuel price, wage and depreciation charge increases. The major expense reductions were in the areas of road maintenance and equipment maintenance and reflect the net impact of reduced traffic levels, a one month strike, and a number of management initiatives to contain costs and maximize operational efficiency. The sizable capital programs in 1990 and previous years have resulted in efficiencies which should limit future operating costs.